

City of Detroit

CITY COUNCIL

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TO: COUNCIL MEMBERS

FROM: Irvin Corley, Jr., Director *ICJ*

DATE: January 31, 2007

RE: Status of Current Lease for Cobo Arena and Joe Louis Arena

Council asked that I provide some financial information regarding the lease between the City and Olympia Arenas, Inc. ("Olympia") for the Cobo Arena and Joe Louis Arena facilities. That information is provided under the section "Financial Information Regarding Rent, Additional Payments and City Ticket Service Fee Received Under the Olympia Sublease" on page 5 of this report.

However, I thought it would be helpful also, to provide some background information on the City's parking system, which includes the arenas, and the Olympia Sublease, including the term of said sublease.

Background

The Detroit Building Authority ("DBA") owns the City's municipal parking system. The parking system includes the **Joe Louis Arena and garage, Cobo Arena and garage** and approximately 14,358 parking spaces located as follows: approximately 9,018 spaces in ten parking garages, approximately 840 spaces in two public parking lots, and approximately 4,500 spaces serviced by on-street parking meters. Appendix I gives some historical information and more detail on the parking system.

The City leases the parking system from the DBA via a Contract of Lease entered into by the parties in 1978. The Contract of Lease term is from July 1, 1978 to June 30, 2008, unless extended by additional outstanding bonds, but no later than June 30, 2028.

The City, through its Municipal Parking Department, controls the vehicular parking activities of the parking system, through contracts and parking management companies to operate the garages and lots and by managing the parking meters itself.

The City retains control over the parking rates, days and hours of operation of each parking facility, and is responsible for major repairs and replacements to the garages and lots.

Cobo and Joe Louis Arenas

Cobo Arena and Joe Louis Arena, built in 1961 and 1979, respectively, are entertainment facilities owned by the DBA and leased to the City.

Cobo Arena is a companion facility to Cobo Hall, the City's major multipurpose convention facility, and is connected to the main level of Cobo Hall. It provides seating for approximately 12,000, including 9,561 permanent, theatre-style seats in three tiers and accommodates concerts, boxing and wrestling matches, basketball games, and various other events.

Joe Louis Arena was added to Detroit's convention/entertainment complex in 1979 at a cost of approximately \$30.3 million. It is located on the Detroit River near the City's Civic Center and seats 19,100 for hockey and up to 2,000 more for other events. In addition, there is a private loge level consisting of private suites and an exclusive clubroom.

The Detroit Red Wings hockey team is the major tenant at Joe Louis Arena. The hockey team is obligated to play all regular season and playoff home games there until 2008, per under the Olympia Sublease, which is described below.

Nature and Term of the Olympia Sublease

The City entered into a 30-year master lease with Olympia ("Olympia Sublease") on August 16, 1978. So technically, the sublease expires on August 16, 2008.

Under the Olympia Sublease, Olympia has full authority to manage and operate the Cobo and Joe Louis arenas. After the initial term of 30 years, the Olympia Sublease **automatically renews for 20 years**. The sublease would operate under the 20-year renewal on the same terms generally as under the initial term of the lease, except that

- a) Olympia is obligated to pay any and all real property taxes without reimbursement thereof during such renewal,
- b) No ticket service fee may be imposed and
- c) Except with respect to the first five years of such renewal, the City does not share in the concessions, novelties or private suite rentals as described below in the section "Additional Payments from Olympia Under the Olympia Sublease".

Additionally, Olympia would have the **automatic right** to a second renewal of the sublease on the same terms and conditions as the first renewal for an **additional ten-year period**.

So, in essence, Olympia has the sole right to a renewal of the Olympia Sublease for up to an additional 30 years after August 16, 2008.

Under the Olympia Sublease, if Olympia desires not to extend the initial term of the sublease for any additional term as described above, then it must inform the City in writing no less than 12 months prior to the end of the initial 30-year term, or on August 16, 2007, of such decline.

So, if the City does not receive any written notice from Olympia on August 16, 2007, then Olympia could automatically receive a 20-year and then a 10-year extension of the sublease after the initial 30-years. Or, Olympia could provide the City a written notice on August 16, 2007 stating its desire not to receive an automatic 20-year and 10-year extension. Or, Olympia could provide in writing that it accepts the automatic 20-year renewal, but declines the 10-year renewal period.

Termination of Olympia Sublease

Article 17 of the Olympia Sublease addresses termination of the sublease. Essentially, Article 17 states that neither party, the City nor Olympia, has a right to terminate the sublease **prior to the commencement date of the initial term (30 years)** except

- a) There is a change in the U.S. Constitution or State Constitution, or there is a federal or state legislative or administrative action, that mandates termination of the lease, or
- b) There is a final judgment in the court of law, either federal or state, that declares termination of the lease, or
- c) Olympia could terminate the lease if Joe Louis Arena and parking garage would not be "substantially complete" by January 1, 1982. (Note: as mentioned previously, the Joe Louis facility was completed in 1979.)

Beyond the commencement date of the sublease, which was August 16, 1978, there appears to be no language that allows for termination rights for the City. The Council may wish to have Research and Analysis Division and the Law Department give you an opinion to substantiate my layman opinion of this.

And again, it appears only Olympia has exclusive rights to renew the lease or not beyond the initial 30 years of the sublease, which ends August 16, 2008.

Rent Under the Olympia Sublease

Olympia rents the arenas for \$450,000 per lease year, payable in equal monthly installments of \$37,500. \$150,000 is attributed to Cobo Arena and \$300,000 to Joe Louis Arena.

All real property taxes are paid by Olympia, except that during the initial 30-year term of the Olympia Sublease, if the real property taxes on the arenas exceed the aggregate of \$252,000 in any given tax year, the City will be required to reimburse Olympia for the amount of the excess.

Additional Payments from Olympia Under the Olympia Sublease

The Olympia Sublease was amended a second time in 1991 to codify the additional payments the City receives from Olympia from the operations of the Cobo and Joe Louis arenas.

During the initial term of the Olympia Sublease and for the first five years of the initial 20-year renewal term, the City also receives in addition to the rent described above

- a) 10% of the gross revenues received from food sales in the arenas (excluding the executive lounges, private boxes or similar private areas),
- b) 5% of the gross revenues received from the sale of novelties, programs, T-shirts, clothing and souvenirs sold in the arenas, and
- c) 10% of the gross revenues received from the sale of beverages in the arenas including sales from areas excluded in a) above (but only, in each instance, in connection with events held in the arenas).

In addition, the City is entitled to receive 25% of the gross revenues received by Olympia in any one year in excess of \$750,000 from the sale of subscription, pay or cable television rights to "live events" held in the arenas, but only if such gross revenues exceed \$1,000,000 in that year.

Olympia is responsible for paying the additional amounts due to the City on a quarterly basis. Council may wish to ask the Auditor General's Office when is the next scheduled audit of Municipal Parking and that you want the AG to audit Olympia's books regarding submission and accuracy of concession revenue and timeliness of deposits.

The City's right to receive the foregoing percentages of revenues derived from sales of food, novelties, beverages, and its right to receive a percentage of revenues from the sale of television rights, expires at the end of the initial term of the Olympia Sublease (2008) or, if the Olympia Sublease is renewed, at the end of the fifth year of the initial renewal term (2013).

City Ticket Service Fee Under Olympia Sublease

The City imposes ticket service fees equal to 10% of the selling price of the ticket on every paid admission for events held at the Joe Louis Arena and 7.5% of the selling price (which the City may increase to 10%) on all paid admissions for events held at Cobo Arena, but in no event less than \$0.50. In certain limited circumstances additional ticket service fees may be charged.

The fee imposed on private suites in Joe Louis Arena (which are leased on an annual basis without regard to individual events) is equal to 6-2/3% of the actual annual cash proceeds received by Olympia for such suites.

Olympia is responsible for paying the ticket service fees from events to the City on a weekly basis. Private suite service fees are to be paid quarterly. Council may wish to ask the Auditor General's Office when is the next scheduled audit of Municipal Parking and that you want the AG to audit Olympia's books regarding submission and accuracy of ticket service fee revenue and timeliness of deposits.

The City's right to receive ticket service and private suite fees expires at the end of the initial term of the Olympia Sublease (2008) and may not be renewed by the City.

Financial Information Regarding Rent, Additional Payments and City Ticket Service Fee Received Under the Olympia Sublease

Financial reports prepared by Municipal Parking Department and Rich and Associates, Inc., financial consultants for MPD, were obtained. Based on this information, arena rentals, ticket surcharge fees, concessions and private suite fees for the years 2002-03 through 2006-07 are as follows:

	<u>FY 2002-03</u>	<u>FY 2003-04</u>	<u>FY 2004-05(1)</u>	<u>FY 2005-06</u>	<u>FY 2006-07(2)</u>
Arena Rentals	\$450,000	\$450,000	\$450,000	\$450,000	\$450,000
Ticket Surcharge	\$2,248,800	\$2,330,300	\$456,040	\$2,510,300	\$2,569,100
Concessions and Private Suite Fees	\$2,336,100	\$1,813,000	\$2,072,600	\$1,642,600	\$1,998,800

(1) Revenue significantly lower in 2004-05 due to NFL hockey strike.

(2) 2006-07 figures are projected.

MPD recalculates figures to ensure they represent percentages in accordance with the Olympia Sublease provisions. However, there is very little auditing done to ensure the base revenues (such as the number of tickets sold, the number of hot dogs sold, the number of drinks sold, etc.) are correct.

Again, the Auditor General needs to review Olympia's books to ensure correct amounts are being remitted to the City, and that they are remitted timely.

Council should note too that there is a late payment provision, whereby Olympia is responsible for paying to the City a daily interest rate of 1-1/2% on any rent, concession fees, and ticket service fees not remitted to the City when due. Olympia is responsible for arena utility payments as well, according to the sublease. Payments are due as follows:

	<u>Payment Due Date</u>	<u>Olympia Late Payment Beginning Date for Interest</u>
Rent	1st day of the month	2nd day of the month
Concession	30 days after the end of each calendar quarter	31 days after the end of each calendar quarter
Utilities	30 days after the date of mailing of invoice by City	31 days after the date of mailing of invoice by City
Ticket Service Fee	Tuesday after event (paid on Monday)	Second Tuesday after event

It is not clear whether Olympia has followed this provision of the sublease. The Auditor General should check this.

Pledge of Rent, Additional Payments and City Ticket Service Fee Received Under the Olympia Sublease

In accordance with the Contract of Lease between the City and DBA regarding the City's parking system, including Joe Louis and Cobo arenas, gross revenues from the parking system are pledged for the payment of "basic rent".

"Gross revenues" include

- a) Fees for vehicle parking (from garages, lots and meters)
- b) Investment earnings on funds and accounts held under the bond resolution and Contract of Lease
- c) **Annual rental payments from Olympia of \$450,000 pursuant to the Olympia Sublease (described above)**

- d) **Ticket service fees on all paid admissions for events held in the arenas (7.5% in Cobo Arena and 10.0% in Joe Louis Arena-described above)**
- e) **6.6% of private suite rental fees in Joe Louis Arena (described above)**
- f) **10% of gross concession sales and 5% of gross receipts from novelty sales from both arenas-described above).**

To secure payment of the "basis rent", the Contract of Lease provides that the gross revenues are first required to be deposited into the City's Revenue Fund on a daily (as far as practicable) basis. "Basic rent" is described in the Contract of Lease as:

- Payment of Principal and Interest (debt service) on any outstanding bonds associated with the parking system,
- Payment into the Debt Reserve Account to satisfy the Debt Reserve Account requirement,
- Payment into the Operating and Contingency Reserve Fund to satisfy the Operating and Contingency Reserve Fund requirement,
- Payment into the Credit Enhancement Fee Account, if necessary, to pay credit enhancement fees for the parking bonds,
- Payment into the Service Charge Account, if necessary, to cover service charges with any outstanding variable rate parking bonds,
- Payment into the Operating and Maintenance Reimbursement Fund for the amount needed to reimburse the City for operating expenses of the parking system, and
- Payment into the Surplus Fund any balance in the Revenue Fund (subject to certain minimum balances to be retained in the Revenue Fund; more specifically, any amount in the Revenue Fund will not exceed 10% of the budgeted parking system operating expenses). Any amounts in the Surplus Fund can be used to help other accounts and funds mentioned above meet balance and reserve requirements. Monies in the Surplus Fund can be used to cover capital expenditures associated with the parking system, including the Joe Louis and Cobo arenas, as well.

Currently, there are no funds in the Surplus Fund.

In addition, pursuant to Act 31, which governs the establishment of the DBA, the bond resolution associated with the parking system bonds creates a lien constituting a statutory lien upon the gross revenues pledged for payments of "basic rent" made by the City under the Contract of Lease in favor of the bondholders. Act 31 and bond resolution furthermore provide that the payments of "basic rent" will remain a statutory lien until the payment in full of outstanding parking system bonds. Outstanding parking system bonds are expected to mature in 2029. The "basic rent" pays off any parking system bonds, and

therefore, the bonds neither are not general obligations of the City nor are secured by the full faith and credit of the City.

So, in essence, none of funds from gross revenues of the parking system are available for deposit into the City's General Fund until outstanding debt associated with the parking system is paid off.

Maintenance of Joe Louis and Cobo Arenas Under the Olympia Sublease

Olympia is responsible for maintenance of the arenas at its own expense; the City, however, is responsible for snow removal, landscape work and other service around certain areas of Cobo arena. The City can inspect the arenas for maintenance purposes or for violation of laws affecting the public health, safety and welfare.

The Olympia Sublease stipulates that the City provides police services for the arenas at its sole cost. However, normal City police services are not interpreted to usurp services provided by ushers and private security personnel.

Reimbursement of Capital Expenditures per Joe Louis and Cobo Arenas Under the Olympia Sublease

The Olympia Sublease provides a mechanism to reimburse Olympia for certain capital improvements made to the arenas, which are not the responsibility of Olympia, but only to the extent amounts are available in the parking system's Surplus Fund.

The intent of this reimbursement for these expenditures is to allow Olympia to compete more effectively for musical concerts to be held in Joe Louis and Cobo arenas.

The sublease provides that the amount of such reimbursements is limited to the lesser of \$500,000 annually, or the amount of the City ticket service fees received the preceding calendar year on musical concerts.

Warrant of Hockey Games Played at Joe Louis Arena Under the Olympia Sublease

Under the Olympia Sublease, Olympia covenants that the Detroit Red Wings Hockey Club will play all regular season and playoff home games at Joe Louis Arena. Olympia has a sublease with the Red Wings, which codifies this agreement.

In the event the hockey club fails to play all scheduled home games at the Joe, the Red Wings are required to pay any accelerated bond payments to keep the parking system's outstanding debt obligations whole.

The City's Right to Use Arenas Under the Olympia Sublease

The Olympia Sublease provides to make either Cobo Arena or Joe Louis Arena available for the use of conventions scheduled by the City if, (i) the use of one or both of the arenas is necessary for the convention and (ii) Olympia is notified of this request by the City at least one year in advance of the date the particular arena is to be used. Olympia also agrees to make the arenas available to the City each year for a total of 50 events involving public school or other civic non-profit functions if the use of the arenas will not conflict with scheduled or known but unscheduled future events.

Olympia will be entitled to charge for its expenses of opening and operating the arenas during these events.

Parking Agreement Under the Olympia Sublease

Pursuant to the Olympia Sublease, Olympia has a separate Operating and Management Agreement with respect to the Joe Louis Arena garage, the term of which runs concurrently with the Olympia Sublease, including renewal periods.

Under the agreement, Olympia operates the garage and deposits the gross revenues directly into an account established by and for the City. The City is responsible for setting rates, establishing hours of operation and paying all operating and maintenance expenses of the Joe Louis Arena garage incurred by Olympia.

Olympia is entitled to the use of 50 spaces in the Joe Louis Arena garage at all times without charge as compensation for operating and managing the garage.

Any Sale and Demolition of Joe Louis and Cobo Arenas

As Council knows, there have been talks about a proposal from Wayne County Executive Robert Ficano to expand and upgrade Cobo Center. His plan calls for demolishing Cobo Arena and expanding exhibit space in the convention center by nearly 40% to 970,000 square feet. Obviously, this proposal is just at the discussion stage, and it would require Council approval if it ever became a real proposal.

In addition, it is not known whether Mike Illitch would seek to build a new hockey arena at another location in the City once the initial term of the Olympia Sublease expires in 2008.

At any rate, if either the Joe Louis Arena or Cobo Arena is sold and/or demolished as a result of any future event, such as is speculated above, the

parking system would have to made whole in order to provide sufficient revenues to pay the "basic rent" as described above.

Of course, any arena facility, land and appurtenances located thereon would have to be sold at fair market value.

Conclusion

The Olympia Sublease is a document strongly in favor of Olympia. The initial term of the sublease ends in August 2008, and it will be interesting how negotiations will take place, if any, between the City and Olympia regarding the renewal periods of the lease. Any negotiations would start in August 2007.

Meanwhile, certain revenues (rent, concessions, ticket service fees, etc.) generated by the Joe Louis Arena and Cobo Arena are pledged solely to pay off parking system bonds and help meet other fund and reserve requirements in accordance with bond covenants. The accuracy and timeliness of depositing these revenues should be audited by the Auditor General's Office during its next scheduled audit of the Municipal Parking Department.

Appendix I-The Parking System

cc: Council Divisions
Auditor General's Office
Ombudsperson's Office
Ronald Ruffin, Municipal Parking Department Director
Shawny DeBerry, MPD Deputy Director
Roger Short, Chief Financial Officer
Donita Crumpler, General Manager-Finance
Pamela Scales, Budget Director
Ron Chenault, Budget Team Leader
Kandia Milton, Mayor's Office

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Appendix I

The Parking System

In 1999, the City's municipal parking system includes the Joe Louis Arena, Cobo Arena and approximately 17,388 parking spaces located as follows: approximately 10,050 spaces in nine parking garages, approximately 2,322 spaces in five public parking lots, and approximately 5,016 spaces serviced by on-street parking meters.

In January 2007, the City's municipal parking system includes the Joe Louis Arena, Cobo Arena and approximately 14,358 parking spaces located as follows: approximately 9,018 spaces in ten parking garages, approximately 840 spaces in two public parking lots, and approximately 4,500 spaces serviced by on-street parking meters.

The parking garages are comprised of

* Millennium garage	600 Spaces
* Cultural Center garage	330 Spaces
* Eastern Market garage	300 Spaces
* Ford Underground garage	750 Spaces
* Grand Circus garage	900 Spaces
* Premier garage	1023 Spaces
* Cobo Arena garage	345 Spaces (1)
* Cobo Hall garage	570 Spaces
* Cobo Roof garage	1200 Spaces
* Joe Louis Arena garage	<u>3000</u> Spaces (2)
Total	9018 Spaces

The parking lots are comprised of

* Woodward lot	600 Spaces
* Cadillac Farmer lot	<u>240</u> Spaces
Total	840 Spaces

Notes and challenges for the current parking system:

(1) Municipal Parking made repairs at Cobo Arena garage to open 160 spaces to the public for the 2007 auto show. Additional repairs are needed to make the remaining 185 spaces available to the public.

(2) DTE Energy formerly utilized 1,200 spaces from Joe Louis Arena garage. However, on December 31, 2006, DTE started renting 1,200 of the MGM garage attached to its permanent casino project.

Other:

- Planning and Development owns 604 Abbott lot, which contains 350 spaces. PDD is attempting to sale the lot. Therefore, Municipal Parking is no longer receiving revenue from this lot.
- The Detroit Economic Growth Corporation (DEGC) owns the Woodward lot. Municipal Parking captures the revenue from this lot, but the DEGC has a right to make the lot available for economic development purposes, which would delete it from Municipal Parking's sources of revenue.
- First and Bagley garage was sold to DTE Energy for \$1.5 million in 2005-06. The garage was losing money and was in need of extensive repairs. This garage contained 1,200 spaces.
- Greektown garage was sold in May 2006 for \$32 million to Greektown Casino, LLC. It was Municipal Parking's highest grossing parking structure. It contained 1,250 spaces. Greektown Casino is planning to build a 13-story 5,200 space garage in its place and build a 20-22 story hotel tower on top of the new garage. Municipal Parking's consultant Rich & Associates opined that the garage could be removed from the parking system for the agreed upon sale price without harm to the system and without causing the City to be in default of its obligations and covenants under the bond financing instruments by which the parking system is financed.